



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **201216040**
Release Date: 4/20/2012

Date: January 26, 2012

UIL: 501.00-00
UIL: 501.03-30
UIL: 501.32-01
UIL: 501.33-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code § 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law, and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Because you do not qualify for exemption as an organization described in § 501(c)(3), donors may not deduct contributions to you under § 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under § 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: December 6, 2011

UIL: 501.00-00
UIL: 501.03-30
UIL: 501.32-01
UIL: 501.33-00

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

<u>State</u>	=	*****
<u>President</u>	=	*****
<u>Corporation</u>	=	*****
<u>LLC</u>	=	*****
<u>Medical Program</u>	=	*****
<u>Portal</u>	=	*****
<u>Tech</u>	=	*****
<u>Web Address</u>	=	*****
<u>Vice President</u>	=	*****
<u>\$x1</u>	=	*****

Dear :

We have considered your application for recognition of exemption from Federal income tax under § 501(a) of the Internal Revenue Code. Based on the information provided, we have concluded that you do not qualify for exemption under § 501(c)(3). The basis for our conclusion is set forth below.

Facts:

You were incorporated under the laws of State. Your Articles of Incorporation provide that you are organized for the "national implementation project management organization for the [Medical Program] to solve the national health information exchange and adoption of electronic health records." Your Articles do not contain a prohibition on inurement, nor do they contain a clause disposing of your property and assets upon dissolution.

You were founded by President. President is also president of Corporation and the managing partner and chief executive officer of LLC.

You described your primary activity as the national implementation of Medical Program. Medical Program belongs to LLC. You included LLC's Business Plan to further explain your activities and purpose. "The [LLC]'s solutions for the Healthcare/Medical Sector are provided under the brand and program called [Medical Program]. This program is [LLC]'s approach to help reactivate the US Economy through the Healthcare/Medical Sector and to enhance such sector"

You stated that your activities consist of the following:

- Applying for federal and state grants to fund the initial implementation efforts of Medical Program until it becomes self-sustained;
- Managing the relationship with the states' committees for health information exchange (HIE) and adoption of electronic health records (EHR) and corresponding Regional Exchange Centers from all 50 states;
- Marketing and sales of the Portal for all medical professionals;
- Marketing and sales of the advertisement program for funding generation purposes;
- Managing the relationship with vendors to properly enroll all EHR database holders and medical professionals into the medical group with the purpose of allowing HIE and adoption of EHR.

You stated that your activities will generate economic development when implementing the Medical Program in the following ways:

- Generate technology jobs created by LLC and each Tech partner.
- Generate advertisement jobs created by the advertisement program.
- Hosting of the group cloud management system, comprised of all portals will be under LLC, which will require LLC to expand datacenter facilities, leading to construction projects.
- Portal will be sold to medical professionals based on subscription access; Tech partners will develop mini-apps for Portal to be purchased by medical professionals.
- To access Portal, medical professionals will require a browser device; LLC is developing strategic partnership with hardware developers to provide these devices bundled with Portal to medical professionals.
- Medical professionals and patients will access Portal to participate in blogs and discussion forums; these individuals will see the advertisements on each Portal by the advertisement program; these individuals will read these advertisements, find out more about the products and services, and ultimately purchase these products and services.

Corporation is an investor and incubator of the cloud computing technology that lead to Medical

Program. President owns the intellectual property of that technology. You stated that through Corporation, you will have access to a worldwide network of enterprise resource planning implementation consulting companies that will help with the national implementation of Medical Program.

LLC provides access to cloud management systems and group cloud management systems. LLC will host a group cloud management system comprised of all Portals related to Medical Program. LLC has a partner for growth program under the brand Tech, which enrolls internet consultants, value added reseller, authorized consultants, and referral partners.

You anticipate generating revenue solely from gifts, grants, and contributions. You plan to engage in government grant solicitation. You stated that as part of the process in applying for government grants, you "need to establish a 501(c)3 not-for-profit organization. This is the reason of [your] creation . . . and the reason of this 501(c)3 application submission." You have in place the advertisement program, which will allow corporations to advertise in each Portal. The revenue will be used to sustain Medical Program. You also have in place a benefactor program, which will allow any private company or individual to donate funding for the implementation of Medical Program.

In LLC's Business Plan, it says, "[LLC] needs the support of the US Government and initial funding from the ARRA to promote the [Medical Program] in the entire nations."

You anticipate expenses will include those for the compensation of officers, directors, and trustees; other salaries and wages; and professional fees. President and Vice President are both compensated an estimated \$x1 per year for their services on the board. LLC is listed as an independent contractor who will make more than \$50,000 per year in Part V of your Form 1023. You stated that LLC's compensation amount will be by the ARRA grant obtained.

LLC provides access to cloud management systems (CMS) and group cloud management systems (GCMS). LLC will host Medical Group, a GCMS comprised by all Portal related to the Medical Program. LLC has a partner for growth program under the brand Tech in which it enrolls internet consultants, value added resellers, authorized consultants, and referral partners.

President will own all intellectual property on the patents applications submitted to the United States Patent and Trademark Office and Medical Program.

Your Web Address, is one page on LLC's website.

Your Bylaws provide that you shall be governed by a board of directors consisting of three members, together with the officers, at least one of which shall be a resident of the state of Florida and a citizen of the United States. The Bylaws further provide that no officer shall be entitled to receive any compensation for services as an officer. You have the following three board members and officers:

- President
- Vice President
- Corporation, which is listed as your vice president

You have not adopted a Conflict of Interest Policy. When asked what procedures you will follow

to assure that persons who have a conflict of interest will not have influence over their own compensation, you replied, "[T]here is not and there will be no conflict of interest." Additionally, you gave the same response when asked what procedures you will follow to assure that persons who have a conflict of interest will not have influence over you regarding business deals with themselves.

You submitted with additional information, "[t]he reason why [we] need to be a 501c3 is because the company is applying for ARRA funds from the Office of National Coordinator from the Department of Health and Human Services (Federal Government). Part of the requirements of the Grant is to be a 501c3 organization."

Law:

Section 501(a) provides that an organization described in subsection (c) is exempt from income taxation.

Section 501(c)(3) provides for the exemption from federal income tax of organizations that are organized and operated exclusively for charitable, scientific or educational purposes, or for the prevention of cruelty to children, provided no part of the organization's net earnings inures to the benefit of any private shareholder or individual.

Section 509(a)(1) provides that an organization shall be classified as a public charity and not a private foundation if it is an organization described in § 170(b)(1)(A), which includes organizations that normally receive a substantial part of its support from publicly supported organizations, from a governmental unit, or from direct or indirect contributions from the general public.

Section 1.501(a)-1(c) of the Income Tax Regulations ("regulations") defines private shareholder of individual as a person having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(a)(1) provides that, in order to be exempt as an organization described in § 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(b)(1) provides that an organization is organized exclusively for one or more exempt purposes only if its articles of organization (a) limit the purposes of such organization to one or more exempt purposes and (b) do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in § 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(2) provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. Section 1.501(a)-1(c) defines the words "private shareholder or individual" in § 501 to refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized or operated exclusively for one or more tax-exempt purposes unless it serves a public rather than a private interest. To meet this requirement, an organization must establish that it is not organized or operated for the benefit of private interests, such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(2) provides that the term "charitable" is used in § 501(c)(3) in its generally accepted legal sense. The promotion of health has long been recognized as a charitable purpose. See Restatement (Second) of Trusts, §§ 368, 372 (1959); 4A Scott and Fratcher, The Law of Trusts, §§ 368, 372 (4th ed. 1989); Rev. Rul. 69-545, 1969-2 C.B. 117. The Service has recognized that the promotion of health includes other activities other than the direct provision of patient care. Furthermore charitable includes relief of the poor and distressed, advancing education, and lessening the burdens of government. The service has held that poor and distressed beneficiaries must be needy, in the sense that they cannot afford the necessities of life.

In Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. The Court found that a trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university, and therefore, the association did not qualify for exemption.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court considered the qualification for exemption under § 501(c)(3) of an organization formed to provide consulting services for a fee to nonprofit and tax-exempt organizations in the areas of health and health delivery systems, housing, vocational skills, and cooperative management. In concluding that the organization did not qualify for exemption, the court noted that, "... the critical inquiry is whether petitioner's primary purpose for engaging in its sole activity is an exempt purpose, or whether its primary purpose is the nonexempt one of operating a commercial business producing net profits for petitioner Factors such as the particular manner in which an organization's activities are conducted, the commercial hue of those activities, and the existence and amount of annual or accumulated profits are relevant evidence of a forbidden predominant purpose."

In Federation Pharmacy Services, Inc. v. Commissioner, 72 T.C. 687 (1979), aff'd, 625 F.2d 804 (8th Cir. 1980), the court held that, while selling prescription pharmaceuticals to elderly persons at a discount promotes health, the pharmacy did not qualify for recognition of exemption under § 501(c)(3) on that basis alone. Because the pharmacy operated for a substantial commercial purpose, it did not qualify for exemption under § 501(c)(3).

P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), held that an organization that

raised money for college scholarships from the operation of bingo games on the premises of a lounge was not exempt under § 501(c)(3). Three of the organization's five board members were the two owners and an accountant/director of the lounge. The court stated that more than an insubstantial purpose of the taxpayer's activities was to attract persons, by way of the bingo games, onto the premises of the lounge expecting that they would purchase food and beverages while participating in the games. In fact, the court continued, the taxpayer's activities were, in substantial part, designed to enhance the profitability of the lounge. To ensure this result, the articles of incorporation of the taxpayer named three of its five directors as owners or directors of the lounge, with subsequent directors to be appointed by the board of the lounge. Therefore, the board was and always would be controlled by the directors of the lounge. Consequently, all of petitioner's fundraising activities could be controlled by the owners of the lounge to provide them with maximum benefit. Even though the taxpayer and the lounge kept separate accounts and no cash payments were made from the taxpayer to the lounge for rent or wages, the activities of the two were so interrelated as to be functionally inseparable.

In Church by Mail, Inc. v. Commissioner, 765 F. 2d 1387, 1392 (9th Cir. 1985), aff'g T.C. Memo 1984-349 (1984), the court, in affirming the Tax Court's finding that it was unnecessary to consider the reasonableness of payments made by the applicant to a business owned by its officer, stated, "[t]he critical inquiry is not whether particular contractual payments to a related for-profit organization are reasonable or excessive, but instead whether the entire enterprise is carried on in such a manner that the for-profit organization benefits substantially from the operation of the Church."

American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the court defined private benefit as "nonincidental benefits conferred on disinterested persons that serve private interests."

International Postgraduate Medical Foundation v. Commissioner, 56 T.C.M. (CCH) 1140 (1989), an organization, whose activity was to conduct continuing medical education tours abroad, exclusively used one for-profit travel agency to arrange its travel tours. The same individuals controlled both the organization and the for-profit travel agency, and the organization did not solicit bids from any other travel agency. Furthermore, both entities shared the same office. As both entities were interrelated, the Court held that the organization was operated for the benefit of the for-profit travel agency.

Rationale:

We have concluded that you are not organized or operated exclusively to promote health or lessen the burdens of government under § 501(c)(3), or to further any other tax-exempt purpose within the meaning of § 501(c)(3) and § 1.501(c)(3)-1(d). Rather, you are operated primarily for a non-exempt purpose—to apply for and receive federal grant money for the benefit of LLC, a related for-profit entity. Any public purposes for which you may operate are only incidental to this primary nonexempt purpose. In addition, you are operated primarily to provide substantial private benefit to your board members, which is prohibited by § 1.501(c)(3)-1(d)(1)(ii). Therefore, we cannot recognize you as an exempt organization under § 501(c)(3).

Organizational Test

Section 1.501(c)(3)-1(a)(1) provides that, in order to be exempt as an organization described in § 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt. Furthermore, no part of the organization's net earnings may inure to the benefit of any private shareholder or individual.

You do not meet the organizational test to qualify for recognition of tax exempt status under § 501(c)(3). Your Articles of Incorporation do not limit your purposes to one or more exempt purposes as required in § 1.501(c)(3)-1(b)(1)(i). Moreover, you fail the organizational test because your Articles of Incorporation do not dedicate your assets to an exempt purpose under § 501(c)(3) as required in § 1.501(c)(3)-1(b)(4).

Non-Exempt Purpose

In addition to not meeting the requirements of the organizational test, we also hold that you do not satisfy the operational test requirement to be recognized as exempt under § 501(c)(3). To satisfy the operational test, an organization must establish that it is operated exclusively for one or more exempt purposes. An organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in § 501(c)(3). See § 1.501(c)(3)-1(c)(1). Under the operational test, the purpose towards which an organization's activities are directed, and not the nature of the activities themselves, is ultimately dispositive of the organization's right to be classified as a § 501(c)(3) organization. B.S.W. Group, 70 T.C. at 356-57. The administrative record demonstrates that you are operated to apply for and receive federal grant money for the benefit of LLC, rather than a charitable purpose, which is in contravention of §§ 501(c)(3) and 1.501(c)(3)-1(c)(1).

You stated that as part of the process in applying for government grants, "we need to establish a 501(c)3 not-for-profit organization. This is the reason [for our] creation . . . and the reason of this 501(c)3 application submission." You stated elsewhere in your supporting documentation that you were established to apply for and receive government grants. Additionally, you stated that you are organized and operated to implement Medical Program to help solve the national HIE and adoption of EHRs. Medical Program is the brand and program of LLC. When asked to describe your activities, you described the services and products of LLC. Medical Program and the advertisement program are owned and operated by LLC. In LLC's Business Plan, it says, "[LLC] needs the support of the US Government and initial funding from the ARRA to promote the [Medical Program] in the entire nation."

You were created by President to apply for and receive government grants that you then plan to distribute to LLC, to fund and operate the activities of LLC. Applying for federal grants is not an exempt purpose recognized under § 501(c)(3) or accompanying regulations. Therefore, you are not primarily operated for an exempt purpose and cannot be recognized as exempt from taxation under § 501(c)(3).

Private Benefit

In addition to failing to be organized and operated within the requirements of § 501(c)(3), you also operate to primarily benefit LLC, in contravention of § 501(c)(3) and accompanying regulations. An exempt organization must be organized and operated exclusively for exempt purposes pursuant to § 1.501(c)(3)-1(a). An entity that is organized or operated to serve private rather than public interests cannot be recognized as operating exclusively for exempt purposes. See § 501(c)(3)-1(d)(1)(ii); American Campaign Academy, 92 T.C. at 1065. As the Supreme Court held, the presence of private benefit, if substantial in nature, will destroy the exemption of an organization, regardless of an organization's other charitable purposes or activities. See Better Business Bureau, 326 U.S. at 283. Private benefit has been defined as "nonincidental benefits conferred on disinterested persons that serve private interests. American Campaign Academy, 92 T.C. at 1053. Your business relationship with LLC results in impermissible private benefit to LLC. Therefore, you fail to meet the requirements necessary to be recognized as a tax-exempt organization under § 501(c)(3).

In determining whether an organization's activities confer an impermissible private benefit, the court in American Campaign Academy looked to whether the beneficiaries of the organization's activities are also the parties who founded, fund, and direct the organization. Your activities are actually those of LLC, which is owned and operated by President. Furthermore, the technology is owned by President. In LLC's Business Plan, it says, "[LLC] needs the support of the US Government and initial funding from the ARRA to promote the [Medical Program] in the entire nation."

It is well established that an impermissible private benefit results when for-profit organizations are functionally interrelated with exempt organizations. See P.L.L. Scholarship, 82 T.C. at 200; International Postgraduate Medical Foundation, 56 T.C.M. Here, you and LLC are functionally interrelated. The record shows that both you and LLC were established by the same person, President. President serves on the boards of both you and LLC.

The fact that you operate primarily to benefit LLC is further evident from the multiple benefits to LLC you listed that will result from your activities. You stated that your activities will generate jobs for LLC and its programs. These activities are a substantial non-exempt purposes that defeats exemption under § 501(c)(3).

Based on these facts, we conclude that you are operated for the substantial non-exempt purpose of enhancing the private businesses of your founder. Further, you operate in a manner that serves private purposes and is likely to result in inurement.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Service will consider the failure to protest as a failure to exhaust available administrative remedies. Section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the Service.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to this address:

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations